STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

SBC COMMUNICATIONS INC.,
SBC DELAWARE INC.
AMERITECH CORPORATION,
ILLINOIS BELL TELEPHONE COMPANY
d/b/a AMERITECH ILLINOIS, and
AMERITECH ILLINOIS METRO, INC. **Docket No. 98-0555**

Joint Application for approval of the reorganization of Illinois Bell Telephone Company d/b/a Ameritech Illinois, and the reorganization of Ameritech Illinois Metro, Inc. in accordance with Section 7-204 of The Public Utilities Act and for all other appropriate relief.

BRIEF ON EXCEPTIONS ON RE-OPENING OF THE PEOPLE OF THE STATE OF ILLINOIS, THE COOK COUNTY STATE'S ATTORNEY'S OFFICE AND THE CITIZEN'S UTILITY BOARD

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The People of the State of Illinois, *ex. rel.* JIM RYAN, People of Cook County ("Cook County") *ex rel.* RICHARD A. DEVINE, State's Attorney of Cook County, and the CITIZENS UTILITY BOARD, by Robert Kelter, one of its Attorneys ("Government and Consumer Intervenors" or "GCI"), hereby file this Brief on exceptions on re-opening pursuant to the Section 200.830 of the Rules of Practice of the Illinois Commerce Commission ("ICC" or "the Commission"). 83 Ill. Admin. Code Section 200.830.

1. Summary of Position

Our initial brief on re-opening addressed some of the questions raised by the Chairman of the Commission in a series of letters to the Hearing Examiners as the questions relate to the Joint Applicants' proposed acquisition of Ameritech Illinois. The initial brief on re-opening

also corrected the savings calculation advocated by the People of the State of Illinois's Office, the Cook County State's Attorney's Office and the Citizens Utility Board in this docket.

The Hearing Examiners Proposed Order on Reopening ("HEPO on Reopening" or "HEPOR") fails to adequately address threshold issues regarding the scope of the Proposed Order and then goes beyond the parameters laid out by the Commission's letters. The letters request that parties submit new information and make new arguments regarding the issues outlined in the letters. Instead, the Joint Applicants reiterated old arguments and made new arguments unresponsive to the Commission's questions. The HEPOR erroneously disregards the Joint Applicants' failure to respond to the Commission's specific questions and furthermore improperly considered arguments beyond the scope of these questions in reaching its conclusions.

Chairman Mathias' June 4 letter states: "I as well as Commissioners Kretschmer and Harvill, am troubled by the record regarding the reorganization's effects upon competition…I am therefore interested in reviewing an amended filing from SBC and Ameritech which would provide the Commission considerably more detail and specificity regarding the issues mentioned above. Please find a specific list of issues attached to this letter as Attachment A." The June 4 and June 15 letters therefore make it clear that this is an opportunity for the Applicants to supplement the record with new information, not rehash old arguments.

On the three issues that Governmental and Consumer Intervenors focus on in these exceptions -- savings, competition and enforcement -- the Joint Applicants have provided little or no new information and GCI does not see how the Commission can find that in these areas the Joint Applicants' have cured the deficiencies in the record that prompted the Commissions'

questions.

The People of the State of Illinois, the Cook County State's Attorney's Office and the Citizens Utility Board take exception to the following erroneous factual and legal conclusions contained in the Hearing Examiners' Proposed Order on Re-Opening. Our focus in these exceptions in no way should be taken as agreement with the other provisions of the HEPOR. The HEPOR on re-opening fails to address the concerns behind the various provisions of the statute. As previously argued in our individual briefs, the record in this case demonstrates that the Joint Applicants have failed to prove that the proposed merger meets the requirements of Section 7-204 of the Public Utilities Act ("Act"). Therefore the application, as currently filed should be rejected.

II. EXCEPTIONS

1. SAVINGS

QUESTION NO. 8: Provide a total and complete breakdown detailing the Joint Applicants' estimates of the costs and savings associated with this merger. Explain methodology and assumptions used to arrive at the estimates for overall Ameritech savings, Ameritech Illinois savings, and SBC savings. Explain how these savings are spread between the Ameritech states. Explain the methodology and assumptions used to arrive at the estimates for overall Ameritech costs, Ameritech Illinois costs, and SBC costs. Explain methodology used to calculate the total estimated costs of this merger, including a breakdown of the component figures which add up to total estimate of costs.

1. The HEPOR's analysis of the savings issue fails to address in a meaningful way the Commission's question on savings, in violation of the Section 10-103 of the Public Utilities Act.

The HEPOR, inexplicably, does not address the issue of whether the Joint Applicants adequately responded to the Commission's Question #8 on savings and disregards the concerns that triggered the Commission's questions in the first place. The Commission specifically

directed that the Joint Applicants provide methodology and assumptions used to arrive at estimates for Ameritech Illinois' share of merger costs and Ameritech Illinois' share of merger savings in order to create a complete record on the savings issue. The Commission's question does not merely request the Joint Applicants to turn over existing information, but seems to requires more: they were to produce the information if it did not already exist.

The Joint Applicants, however, chose simply to provide information similar to that previously submitted in the earlier phase of this proceeding. Under cross-examination Ameritech witness Gebhardt admitted that neither SBC nor Ameritech made any efforts to obtain more specific savings estimates after the proceedings were reopened. His explanation was that "…there is no way to do it without the companies actually sitting down and figuring out where these savings are going to occur." But "figuring out where these savings are going to occur" is precisely what Question #8 asked the Joint Applicants to do.

Specifically, the Commission requested "a total and complete breakdown detailing the Joint Applicants' estimate of cost-savings associated with this merger," and then proceeded to itemize the specific points of clarification it requested with respect to the calculation of merger savings and costs, and the apportionment of those savings and costs among SBC, affiliates of Ameritech Corporation, and Ameritech Illinois. The Joint Applicants have made no effort to provide any new information regarding the breakdown of savings other than to put old information on a chart. SBC Ameritech Ex. 3.3, Schedule 1 (Gebhardt Direct on Reopening) Thus, even though Joint Applicants asked the Commission to allow them to amend their Application and to reopen the proceeding, Joint Applicants effectively avoided answering the very concerns upon which the Commission sought additional information, and which was the

basis for the Commission granting Joint Applicants' request. In neglecting to provide the analysis the Commission has deemed it necessary to compile a complete record, the HEPOR's analysis on the savings issue does not amount to a conclusion based upon the record, as required by the Public Utilities Act. 220 ILCS 5/10-103.

2. The HEPOR violates the Public Utilities Act by failing to allocate savings prior to approval of the reorganization, pursuant to Section 7-204(c).

GCI takes exception to the HEPOR's account of record evidence on the savings issue and to its ultimate conclusion that the HEPOR's method of determining savings allocated to Illinois ratepayers is reasonable. The HEPOR improperly neglects to consider some of the most important points raised in the testimony on reopening presented in response to Question No. 8 in the Commission's June 4th letter. Specifically, GCI excepts to the HEPOR's decision to refrain from ruling on the specific amount of savings to be flowed through to ratepayers until the five year review of the Ameritech Alternative Regulation Plan. We further except to the HEPOR's conclusion that the time period during which savings shall continue to be flowed through is limited to three years after closing. We also take exception to the determination that merger-related savings to be flowed through to ratepayers should be restricted to expense and cost savings and that revenue enhancements shall not be included in savings.

The HEPOR errs in concluding that merger-related savings need not be determined until Ameritech's annual alternative regulation filing. This methodology is inconsistent with the legislature's specific directive that the Commission "shall not approve a reorganization without ruling on: (i) the allocation of any savings resulting from the proposed

reorganization." 220 ILCS 5/7-204(c). The Commission's Question No. 8 implicitly recognizes that such information is necessary to issue findings under 7-204(c), by directing the companies to report specific merger-related costs and savings for Ameritech Illinois. The Commission apparently understands that it cannot make the statutorily-required allocation under Section 7-204(c) if it relies upon the estimates the Joint Applicants provided in the earlier phase of the case, namely the estimates based upon SBC's experience with the Pacific Bell merger. The Joint Applicants ignore the Commission's directive and the HEPOR improperly condones their failure.

3. The HEPOR's analysis that merger savings should be flowed through to ratepayers for only three years is contradicted by the record.

The HEPOR incorrectly concludes that three years is adequate to flow through merger-related savings to ratepayers. The HEPOR ignores the fact that no record evidence exists to support the notion that "three years represents a reasonable time frame given the state of competition in Illinois." HEPOR at 86. (220 ILCS 5/10-102) As GCI argued in its Intial Brief on Reopening, Mr. Gebhardt admitted on cross examination that there is no study, documents, nor any evidence whatsoever, other than his personal opinion, that would indicate that competition in Illinois will arrive within three years of the merger closing date. GCI Brief on Reopening at 9, Tr. 2110.

The HEPOR also appears to dismiss the fact that the synergy benefits of this merger, if it is approved, will continue to accrue for years to come. Under GCI witness Selwyn's present value method, the totality of merger savings allocable to Illinois intrastate, regulated services is determined over the entire time frame within which those savings would continue to be

realized by Joint Applicants. Id. at 21.

The HEPOR also errs by accepting the Joint Applicants truncated analysis of savings allocable to Illinois. The HEPOR fails to recognize that Joint Applicants only considered net expense and capital savings over the initial three year time period, when their own financial advisers have based their respective valuations of the transaction and fairness opinions upon the continuation of such savings for an indefinite period of time. Amended Joint Proxy Statement, September 21, 1998, at 35, GCI Ex. 1.2 at 8 (Selwyn Dir. on Reopening). Additionally, the Joint Applicants' analysis gives no consideration to significant synergy benefits which are likely to occur over time, such as the increased productivity of the Ameritech Illinois network, or to allocation of certain Illinois costs to competitive and nonregulated services. GCI Ex. 1.2 at 9.

Most significantly, the HEPOR fails to recognize that under Joint Applicants' approach, merger savings realized by the Applicants beyond the third year following the merger closing *are ignored entirely*. Id. No attempt is ever made to establish the present value of all future, merger-driven savings. Id. Nothing in the statute or in its application permits such truncation, and for that reason (as well as its fundamental unfairness to Illinois ratepayers) the Commission should reject Joint Applicants approach. Therefore, the HEPOR errs by accepting it.

The HEPOR further ignores record testimony and arguments that prove the contrary: that three years is not a reasonable time-frame, and that a more correct approach properly takes into account the fact that merger savings will continue to accrue indefinitely beyond the first three years of the merger. GCI Brief on Reopening at 8. The HEPOR also ignores record

evidence showing that the correct and prudent course of action would be to apply a ten year amortization period for flowing savings through. GCI 1.2 at 21 (Selwyn Dir. On Reopening.).

4. The HEPOR errs in reaching its conclusion on the meaning of "savings."

GCI excepts to the HEPOR's conclusion that the meaning of savings as intended in section 7-204(c) of the Act is restricted to a reduction in costs or expenses. Id. at 84, 85. In reaching this conclusion, the HEPOR purports to apply the "plain language doctrine." Id. The HEPOR's reasoning is flawed in several respects.

First, the HEPOR appears to apply the plain language doctrine in a vacuum, mechanically reverting to a dictionary definition of savings when it cites Funk & Wagnell's Dictionary without attempting to place the word in its statutory context as the court did in Texaco-Cities, the only legal authority cited by the HEPOR in support of its use of the plain language doctrine: "*Placed in their statutory context*, these terms indicate that the acquisition, management and disposition of the income-producing property must closely relate to the taxpayer's regular trade . . . Texaco-Cities, 182 Ill. 2d. at 271 (*emphasis added*). The court goes on to interpret the words in question in the broader context in which they were used, not merely relying on a dictionary definition as the HEPOR does. Id. The court in Texaco-Cities, then concluded that the appellants' construction of the statute was unduly narrow and that the clause at issue was much broader. Id.

Similarly, the HEPOR errs by applying an unduly narrow construction of the meaning of the word "savings," as used in section 7-204(c). The meaning of the term, "savings" includes merger-related expense savings as well as revenue enhancements. Staff Ex. 1.00 at 19-20 (Marshall Direct). This is true for two reasons. First, under rate-of-return regulation --

the form of regulation used for all Illinois ILECs other than Ameritech -- both merger related savings and revenue enhancements would automatically be reflected in rates following a merger. *See* Staff Brief on Exceptions at 150 (ICC Docket 98-0555, initial proceedings). Any other interpretation would discriminate against other ILECs in favor of IBT, an absurd result. Had the General Assembly intended that IBT receive favorable treatment, it would have explicitly stated so in the Act.

Second, when viewed in its statutory context, as it should be, the word "savings" refers to any savings, not just expense savings. The legislature obviously recognized that Illinois ratepayers have a significant stake in the reorganization of Illinois' public utilities. *See* AG Initial Brief at 34-35 (98-0555 Initial Proceedings). This is evident by virtue of the plain fact that the legislature even enacted section 7-204(c). Nowhere, in the statute, did the legislature restrict those savings to *expense* savings, and it is not the province of the Commission to import such a restriction. Further, it is a well established principle in Illinois law that in seeking the intent of the legislature, courts consider not only the language used, "but the evil to be remedied and the object to be obtained." Inter-State Water Co. v. City of Danville 379 Ill. 41,46, 39 N.E.2d 356,358 (Ill. 1942) (emphasis added); People v. Hughes, 357 Ill. 524, 192 N.E. 551; People v. Giles, 268 Ill. 406, 109 N.E. 273; Pascal v. Lyons, 15 Ill.2d 41, 153 N.E.2d 817, 819 (Ill. 1958); Dewig v. Landshire, Inc., 281 Ill. App.3d 138, 142, 217 Ill. Dec. 266, 666 N.E.2d 1204, 1206 (3d Dist. 1996). The legislature recognized that mergers would produce significant savings via revenue enhancements and efficiency gains and obviously believed that ratepayers should share in such savings.

Thus when properly viewed in its statutory context, the term savings, encompasses

revenue enhancements as well as expense savings. The HEPOR errs by finding otherwise, because to do so is contrary to the plain meaning of the statute. Specifically, such a finding would import a restriction into the meaning of savings not articulated by the legislature. More importantly, in so finding, the Commission would ignore "the object to be obtained," i.e., that Illinois ratepayers fully share in all savings benefits, including revenue enhancements, resulting from the reorganization of the utility.

Finally, the HEPOR, at page 64 wrongly rejects record evidence that the concept of "savings" includes revenue enhancements, arguing that the "plain language" doctrine of statutory interpretation precludes such an expansion. In fact, Webster's New collegiate Dictionary defines "saving" as "the excess of income over consumption expenditures." Using this definition, certainly revenue enhancement associated with the merger fall into such a category. As noted in CUB's Reply Brief in the earlier phase of this proceeding, the Commission can and should accept the portion of total synergies allocated to Ameritech as constituting a composite of all of the sources of such gains – (1) cost savings through elimination of duplication, scale, lower input procurement costs and adoption of each firm's best practices; (2) increased revenues through improved utilization of existing plant; and (3) substantial opportunities for expansion into new markets through exploitation of each firm's customer base, managerial talent, network resources, brand identification, patents, and other assets; all net of implementation costs. GCI Ex. 1.0 at 89.

1. The Commission should rely on evidence presented by GCI on the allocation of savings.

The Joint Applicants have now had two opportunities to provide the kind of meaningful

and specific information in the area of savings to allow the Commission to meet its obligations under Section 7-204(c). This lack of response should lead the Commission to turn its attention to the approach proposed by Dr. Lee Selwyn in this case. The ratepayers should be allocated $471,584,762 in savings now, as contemplated by the statute. GCI Ex. 1.2 at 17. Ratepayers deserve more than empty promises. The Commission should insure that ratepayers receive their allocation of merger savings now, and not be required to fight to obtain this entitlement in some future docket. The Public Utilities Act requires this and the Commission should order it.

In conclusion, the HEPOR fails to properly consider that Joint Applicants offered neither additional information, a more state-specific description, nor any further breakdown of the factors they used in reaching their $31 million allocation of savings to Illinois. GCI Initial Brief on Reopening, 3-8. Indeed, the HEPOR appears to overlook entirely the fact that Joint Applicants' did not meet their burden of proof because they failed to adequately respond to the Commission's specific questions regarding savings. *See* Id. at 5. Indeed, the HEPOR never addresses whether the Joint Applicants responded adequately to the Commission's question on savings.

Proposed Language:

Commission Conclusion and Analysis

> The record demonstrates that the Joint Applicants have not adequately responded to the Commission's concerns expressed in Question 8 relating to the calculation of merger-related savings and costs by Joint Applicants. The Commission requested "a total and complete breakdown detailing the Joint Applicants' estimate of cost-savings associated with this merger," and then proceeded to itemize the specific points of clarification it required with respect to the calculation of merger savings and costs, and the apportionment of those

savings and costs among SBC, various Ameritech Corporation affiliates, and Ameritech Illinois.[1]

The Commission posed this question because the Joint Applicants' prior testimony was lacking in sufficient detail on the method Joint Applicants used for calculating and assigning savings and costs to the various post-merger entities. In this proceeding on reopening, the record indicates that Joint Applicants made little effort to provide new information regarding the breakdown of savings. Rather, Joint Applicants appear to have merely recycled information previously of record. We agree with Staff witness Marshall's assessment that "no additional data regarding savings" has been provided in response to the Commission's request.

The record on Re-opening sheds no further light on the Commission's concerns with respect to savings as articulated in Question No. 8 of our June 4th letter. Joint Applicants failed to adequately respond to these concerns and therefore we continue to reject Joint Applicants recommendations on savings. The Joint Applicants provide no further information, or analysis to support their conclusion that merger-related savings should be flowed through to ratepayers through Ameritech's annual alternative regulation filing. We hold that such a methodology would transgress the legislature's specific directive that the Commission "shall not approve a reorganization without ruling on: (i) the allocation of any savings resulting from the proposed reorganization." 220 ILCS 5/7-204(c).

To properly address the Commission's concerns in Question No. 8, it was incumbent upon the companies to report specific merger-related costs and savings for Ameritech Illinois. We simply cannot make the statutorily-required allocation under Section 7-204(c) based on the estimates the Joint Applicants provided in the earlier phase of this proceeding, namely the estimates based upon SBC's experience with the Pacific Bell merger. We are of the opinion that Joint Applicants have failed to adequately respond to our request for further, more detailed, information on Joint Applicants method of determining their $31 million figure for savings allocable to Ameritech Illinois regulated services. Accordingly, we reject this figure and the Joint Applicants recommendations for savings allocation.

[1] See Question (8) in Attachment A to Chairman Richard Mathias' letter of June 4, 1999 to Hearing Examiners Mark Goldstein and Eve Moran.

Accordingly, we find that the Joint Applicants have failed to present adequate evidence regarding the measure of merger savings in this matter. We therefore reject Joint Applicants position regarding the measure of savings and the allocation of savings to ratepayers.

Further, we disagree with the Joint Applicants that the term "savings" in Section 7-204(c)(i) ~~refers~~ is limited to an actual reduction in costs or expenses. Undefined terms in statutes are to be given their "ordinary and popularly understood meaning." Texaco-Cities Pipeline Service Co. v. McGaw, 182 Ill. 2d 262, 270 (1998). The "ordinary and popularly understood meaning" of "savings" is "the excess of income over consumption expenditures" Webster's Collegiate Dictionary, 10th Edition at 1039 (1993); ~~a reduction in costs or expenses. See Funk & Wagnall's New International Dictionary of the English Language: Comprehensive Edition at 1120 (1987) ("save" means "to keep from being spent, expended or lost; avoid the loss or waste of" and "[t]o avoid waste, become economical") Black's Law Dictionary at 1343 (6th ed. 1990) ("savings" means "economy in outlay; prevention of waste; something laid up or kept from being expended or lost.")~~ Thus, revenue, which is defined as "gross income returned by an investment," Webster's at 1002, clearly is included under the umbrella of savings ~~does not~~ and therefore the plain meaning of savings includes ~~mean~~ generating more revenue.

Not only is Joint Applicants reasoning flawed under their own "dictionary" approach, it is flawed in several other respects. First, Joint Applicants appear to apply the "plain language doctrine" in a vacuum, mechanically reverting to a dictionary definition of savings when it cites Funk & Wagnell's Dictionary without attempting to place the word in its statutory context as the court did in Texaco-Cities: "*Placed in their statutory context*, these terms indicate that the acquisition, management and disposition of the income-producing property must closely relate to the taxpayer's regular trade . . . Texaco-Cities, 182 Ill. 2d. at 271 (*emphasis added*). The court goes on to interpret the words in question in the broader context in which they were used, not merely relying on a dictionary definition as the HEPOR does. Id. The court in Texaco-Cities, then concluded that the appellants' construction of the statute was unduly narrow and that the clause at issue was much broader. Id.

Similarly, the Joint Applicants err by applying an unduly narrow construction of the meaning of the word, "savings," as used in section 7-204(c). The meaning of the term, savings includes merger-related expense savings as well as revenue enhancements. Staff Ex. 1.00 at 19-20 (Marshall Direct). This is true for several reasons. First, under rate-of-return regulation, the form of regulation used for all Illinois ILECs other than Ameritech, both merger related savings and revenue enhancements would automatically be

reflected in rates following a merger. *See* Staff Brief on Exceptions at 150 (ICC Docket 98-0555 initial proceedings). Any other interpretation would discriminate against other ILECs in favor of IBT, an absurd result. Had the General Assembly intended that IBT receive favorable treatment, it would have explicitly stated so in the Act.

When viewed in its statutory context, as it should be, the word "savings" refers to any savings, not just expense savings. The legislature obviously recognized that Illinois ratepayors have a significant stake in the reorganization of Illinois' public utilities. *See* AG Initial Brief at 34-35 (98-0555 Initial Proceedings). This is evident by virtue of the plain fact that the legislature even enacted section 7-204(c).

Further, it is a well established principle in Illinois law that in seeking the intent of the legislature, courts consider not only the language used, "but the evil to be remedied and *the object to be obtained*.", 379 Inter-State Water Co. v. City of Danville Ill. 41,46, 39 N.E.2d 356,358 (1942); People v. Hughes, 357 Ill. 524, 192 N.E. 551; People v. Giles, 268 Ill. 406, 109 N.E. 273 (emphasis added).

The legislature recognized that mergers would produce significant savings via revenue enhancements and efficiency gains. The legislature believed that the ratepayers should share in such savings. Nowhere, in the statute, did the legislature restrict those savings to *expense* savings, and it is not the province of this Commission to import such a restriction into the meaning of savings. Thus, when properly viewed in its statutory context, the term, savings, encompasses revenue enhancements as well as expense savings. We would err in ruling otherwise because to do so would render an absurd result. Specifically, such a finding would import a restriction into the meaning of savings not articulated by the legislature. More importantly, in so finding, this Commission would be ignoring the "object to be obtained," i.e., that Illinois ratepayers fully share in all savings benefits, including revenue enhancements, resulting from the reorganization of the utility. After all, Illinois Bell Telephone Co. was largely built from 100 years of guaranteed returns on investment. Those returns were funded by Illinois ratepayers. We therefore reject Joint Applicants' recommended definition of savings.

~~Looking to the particulars of Section 7-204(c), the plain language doctrine again leads us to construe "savings" as that term is ordinarily understood, namely, a reduction in costs or expenses. Hence, the urgings of Staff and certain Intervenors that we widen the pool to include "revenue enhancements" are rejected. The mere fact that the parties themselves have consistently drawn a distinction between "expense savings" and "revenue enhancements" reaffirms~~

~~our belief that "revenue enhancements" is not what the General Assembly intended when speaking of "savings". Courts are not free either to restrict or to enlarge the plain meaning of a unambiguous statute and we also follow this pronouncement. Ehredt v. Forest Hospital Inc. 142 Ill. App. 3d 1009, 492 N.E.2d 532 (1st Dist. 1986).~~

As for the meaning of "costs", the Commission agrees with Staff that none of the one-time merger costs which relate to the change in ownership of Ameritech, such as banker or brokerage fees, legal fees, or accounting fees, constitute legitimate costs for present purposes. It is only those costs directly associated with AI's provision of service which qualify under Section 7-204(c). Hence, in principle, we agree with Staff's position to allow recovery of only those costs directly associated with the utility's operations. However, we also agree with GCI that due to the Joint Applicants failure to provide sufficient detail regarding costs that would be incurred as a result of the proposed merger, the Commission must deny recovery of *any* costs by Joint Applicants. The Commission is reluctant to deny reasonable cost recovery. However, given the lack of a clear record as to costs incurred, and given that we are bound to render all decisions based only upon record evidence, we have no other choice. Accordingly, we deny Joint Applicants recovery of any costs resulting from the proposed merger.

~~Given the Commission's strong preference for dealing in matters of certainty~~, Consistent with this provision we believe that ~~both~~ the savings ~~and the costs~~ of this transaction as well as their reasonableness, must be determined before the merger is approved using ~~the~~ estimated savings. ~~when actual data, as opposed to estimates, are available. We further note the disparity between the result generated by the Dr. Selwyn and the estimate presented by Mr. Gebhardt, as convincing proof of the need to await actual figures. Moreover, with respect to Dr. Selwyn's savings estimate, we believe that the underlying methodology based largely on the purchase premium paid by SBC for Ameritech is not appropriate for the task. Such an analysis necessarily discounts or excludes the fact that in nearly every transaction of this type there is a multitude of factors and motives underlying both the merger decision and the size of the premium. Because the cost savings of the merger are calculations, at best, only one of the factors taken into account, they simply cannot be equated with the total premium.~~

~~We fully agree with Staff that the Commission needs to make separate rulings on both savings and costs pursuant to Section 7-204(c) requirements. This we intend to do. However, we are not persuaded by Staff's position opposing the netting of savings and costs. To the extent that costs are incurred to produce savings and are shown to be both reasonable and directly related, we~~

~~agree with the Joint Applicants that netting is appropriate. As a matter of logic, the only savings that can be experienced are net savings. Moreover, our reading of Section 7-204(c) indicates that just such a result is contemplated. We further conclude on the arguments presented, that 50% of the net merger savings allocable to AI should be allocated to consumers using Staff's distribution methodology. This strikes a fair balance considering the commitment, performance and benchmark costs which will be incurred post-merger.~~

~~In keeping with our responsibilities under Section 7-204(c) and based on the evidence of record, we direct the Joint Applicants to follow Staff's Interim Method until the appropriate mechanisms are made in the five-year review of the Plan.~~

The Staff's position has merit in that it calls for ratepayers to benefit directly from the synergies associated with this proposed transaction. However, the Staff's proposal that savings be calculated subsequent to the transaction and in the context of Ameritech Illinois' annual rate filings associated with the alternative regulation plan is flawed. Joint Applicants' witness Kahan admitted under cross-examination that the determination of merger-related savings would be virtually impossible three years following consummation of the merger. We find, therefore, that allocation of savings in the manner recommended by the Staff is not feasible and would result in an inadequate allocation of savings to ratepayers. Accordingly, we must reject it.

The Neighborhood Learning Network bases its savings estimate upon a $1.4 billion figure provided by the Joint Applicants. We cannot accept this figure nor do we find NLN's calculation of allocable savings to have the precision and the exactitude that we require. While we share the Neighborhood Learning Network's concerns regarding inequitable access to the telecommunications network and associated computer and information services, we cannot adopt NLN's method of allocation.

In contrast, the savings methodology proposed by the Government and Consumer Intervenors is supported by evidence of record. Further, GCI's approach of allocating savings at the consummation of the proposed transaction has the distinct advantage of conserving the Commission's resources by not requiring that this matter be revisited with each annual rate filing. In addition, we conclude that it will be difficult if not impossible to determine the measure of savings over time after the consummation of the transaction. Thus, we find that allocation of savings at consummation of the transaction rather than through the annual rate filing is the more equitable, economical and realistic approach and we adopt it.

We do not accept the Joint Applicants' estimate of allocable savings in this matter, and the Staff's method presents insuperable administrative problems, as well as practical accounting challenges described above. In contrast, the GCI method of allocating savings based upon evidence of the savings and synergies the Joint Applicants expect to realize from the transaction, has the advantage of premising the savings allocation upon the actual value of the transaction as determined by the commercially sophisticated parties.

In conclusion, we find that Section 7-204(c) of the Public Utilities Act applies to the transaction before us. We further find that merger savings should be allocated at the consummation of the proposed reorganization. Finally, we determine that the sum allocable to ratepayers is $471,584,762.00, as a one time rate decrease to be applied to all noncompetitive Ameritech Illinois services in accordance with the distribution method advanced by the Staff, and to remain in effect for a ten year period.

[Alternative language to reflect 50% allocation]

Finally, we determine that the sum allocable to ratepayers is $235,792,381.00, as a one time rate decrease to be applied to all noncompetitive Ameritech Illinois services in accordance with the distribution method advanced by the Staff, and to remain in effect for a ten year period.

~~To be specific, Ameritech Illinois is required to track its share of all actual merger-related savings and all merger-related costs, as herein defined, separately for the period beginning on the date that the merger is consummated and ending on March 15, 2000. AI shall submit that information as part of its annual Alt. Reg. filing on April 1, 2000. Furthermore, this information will continue to be provided in Ameritech's annual price cap filings until such time as an updated price cap formula has been developed in Docket 98-0252. In the annual price cap filings, AI is required to flow-through merger savings net of reasonable costs in the manner here described for a period of three years. A period of three years represents a reasonable time frame given the state of competition in Illinois.~~

~~It is the ruling of this Commission that the net merger-related savings should be allocated to Ameritech Illinois' customers as follows:~~

~~(1)Carriers purchasing AI's UNEs, interconnection, and transport and termination services will benefit from merger-related savings through updated rates resulting from modification of its TELRIC, shared and common costs.~~

~~(2)Once the share of the merger-related savings allocable to UNEs, interconnection,~~

transport and termination purchasers have been identified, the remaining balance of savings will be allocated to interexchange, wholesale and retail customers. This will be done by dividing the remaining merger-related savings between IXCs on the one hand and end users (whether served via retail or wholesale) on the other, based on the relative gross revenues of each of these two groups.

As per Staff's recommendations, which we find to be reasonable, IXCs' share of the merger-related savings should be allocated to those customers through reductions in access charges, including the intrastate PICC. End users' share of the merger-related savings should be allocated as a credit on a per network access line basis to ensure that business customers do not receive a larger portion of the merger-related savings than residential customers.

2. COMPETITION

QUESTION NO. 1: An explanation of whether SBC is or is not an "actual potential competitor" in Illinois, as the term has been used throughout this proceeding.

1. The HEPOR failed to adequately answer whether SBC was an "actual potential competitor" in Illinois.

Question 1 asks for an explanation of whether SBC is or is not an "actual potential competitor." The question goes no further. The HEPO on Reopening concludes that SBC would likely enter the local market in the next three to five years. HEPOR at 31. Thus, it would appear that the Hearing Examiners conclude that SBC is an actual potential competitor. This is where the Hearing Examiners analysis should stop based on the limited scope of the question. However, the analysis does not stop. The Hearing Examiners then conclude that despite the likelihood that SBC would be a competitor, there will be no effect on the market:

> In the final analysis, while SBC could likely enter the local market in the next three to five years, it is improbable that SBC will be able to single-handedly deconcentrate the market or obtain a significant share of the market anymore than other competitors combination with other entrants.

HEPOR at 31. Thus, the HEPOR apparently finds that the merger meets the standard in subsection (6) that "the proposed merger is not likely to have a significant adverse effect on competition in those markets over which the Commission has jurisdiction." 220 ILCS 5/7-204(6). The HEPOR does not contain sufficient analysis to justify its conclusion on competition, especially given the Joint Applicant's failure to provide additional information. Section II of the HEPOR Purpose and Scope of the Proceeding states that the scope of the proceeding is defined by the letters from Chairman Mathias and the Attachments. The record

on reopening does not on its own support a further conclusion regarding the effect on competition.

There also seems to be some inconsistency in the HEPOR's logic. The HEPOR finds that SBC would in fact be a likely competitor, but that this does not matter in the final analysis regarding the effect on competition under subsection (6). This begs the questions: if SBC's status as a likely competitor is irrelevant to the effect of the merger on competition, why did the Commission ask for an explanation as to whether SBC is or is not an actual potential competitor?

2. The HEPOR incorrectly concludes that SBC is not an "actual potential competitor" **in Illinois, as the term has been used throughout this proceeding.**

Although we believe the record on re-opening does not support a further conclusion on the effect on competition, we are compelled to address this analysis. In our initial brief we address some of the factors that identify SBC as an actual potential competitor, GCI Initial Brief at 11-16. The GCI brief used DOJ guidelines cited at GCI Initial Brief at 11, to assess the ease of entry by SBC into the AI market, yet the HEPOR barely mentions this persuasive analysis in the HEPOR at 24. The HEPOR properly considers the DOJ Guidelines set out by Staff without incorporating the parallel criteria put forth by the GCI as to the timeliness, likelihood and sufficiency of entry into the AI market by SBC.

Proposed Language:

Insert a new paragraph after the second full paragraph on page 25:

The GCI (AG, Cook County and CUB) argue that SBC is an

"actual potential competitor" if it is able to enter the local exchange markets in Illinois absent the merger with sufficient ease. These parties add that entry is easy, pursuant to the DOJ guidelines, if it is "timely, likely and sufficient in its magnitude character and scope."

Recognizing that it is difficult to prove a negative, i.e., that SBC is not an actual potential competitor, the GCI contend that ~~direct evidence is not the only means by which to evaluate~~ the question is easily resolved by noting the ease of entry of SBC into the AI market without this merger. SBC is the most likely competitor ~~There are a number of factors relevant to such an inquiry, GCI argue, which can be examined and which show that SBC would have a tremendous advantage~~ in providing facilities-based local telephone service~~. These factors, as set out by GCI, are SBC's~~ because of experience gained from providing cellular service in Illinois and the wireline service near St. Louis~~)~~, its size and financial strength. According to GCI, the Joint Applicants have not addressed these factors. SBC's entry into the local exchange market would be timely due to SBC's ~~The GCI also point to SBC's~~ desire to become a national and international provider of telecommunications service. SBC would enter the market to a sufficient extent because w~~W~~ith such ambitions, the GCI claim, SBC could not avoid competing for local exchange service in Illinois due to the extensive network of national and multinational corporations located in the Chicago MSA. The attractiveness of the Chicago MSA is, according to GCI, borne out by the number of CLECs who have attempted to offer local exchange services here. These economic factors show that SBC's ease of entry into the AI market without this merger identify SBC as an "actual potential competitor".

~~The CGI (AG, Cook County and CUB) argue that SBC is an "actual potential competitor" if it is able to enter the local exchange markets in Illinois absent the merger with sufficient ease. These parties add that entry is easy, pursuant to the DOJ guidelines, if it is "timely, likely and sufficient in its magnitude character and scope."~~

3. The HEPOR does not properly consider the substantial advantages that SBC would have in competing for the local residential market including marketing and technical expertise in building facilities-based residential service, and market leadership in vertical integration of other residential telephone services.

The HEPOR concludes that SBC's entry would be limited to large business customers, and fails to note the advantages that SBC would have over other potential entrants like AT&T, MCIW, and Sprint. While these CLECs have significant resources, they do not have the marketing and technical experience to build a facilities-based residential service that each RBOC possesses. SBC cannot be expected to forgo such advantages to enter the local residential market within 3-5 years. In addition, both Staff and GCI have suggested that SBC alone among the parties in this matter has the desire and means to provide one stop shopping for telecommunications services, including Caller I.D. and Call Waiting. In defining likelihood of entry, some federal courts require "clear proof" of entry, while others only require a "reasonable probability", see e.g. FTC v. Atlantic Richfield Co., 549 F.2d 289, 294-295(4th Cir 1977); BOC International Ltd. v. FTC, 557 F.2d 24, 28 (2nd Cir. 1977); Mercantile Tx. Corp. v. Board of Governors, 638 F.2d 1255, 1268-1269 (5th Cir. 1981). Such advantages and ambition make an entry by SBC into the residential AI market likely under the DOJ guidelines. Revisions to the HEPOR suggested by GCI below reflect a more thorough discussion of SBC's likelihood of entering the local AI market.

The following changes should be made to pages 27-31:

> Accordingly, we will also consider the other two bases which Staff advanced as reasons why the proposed merger is likely to have an adverse effect on competition, i.e., that the proposed merger is likely to inhibit the market's transition to competition and to increase the market's barriers to entry. In the same vein, we will incorporate the "ease" of entry analysis proposed by the GCI. Not only do we find that Section 7-204(b)(6) requires us to consider these positions; but, these positions were undeniably found to be the means by which mergers of local exchange carriers can have adverse effects on competition by the FCC. Thus, they are suitable areas for our inquiry.
>
> We recognize the general concept that competition only develops when

competitive firms are able to enter a market and expand the supply of good that is being provided. In these premises, Ameritech Illinois' dominant market share must be eroded by the entry of competitive carriers and an expansion of their supply of goods. ~~There is, however, no conclusive evidence to show that the proposed merger will~~ A merger with another RBOC such as SBC can only serve to inhibit the ability of competitive carriers to enter the market and to increase their supply of the goods for local residential service.

~~We also do not believe that the proposed merger will increase the market's barriers to entry preventing competitive carriers from entering or expanding the supply of the goods.~~ This merger poses potential hardships to consumers and CLECs. It has been argued that the barriers to entry will increase in a number of ways, including increasing the level of disparity between the information held by Ameritech Illinois and CLECs, decreasing the amount of information available to consumers about alternative providers to Ameritech Illinois, and resale and UNE prices, increasing resistance to the implementation of our pro-competitive policies, creating an opening for the adoption of anticompetitive practices within Illinois under the guise of best practices, and increasing the company's incentive and ability to discriminate. ~~This, however, is based only on speculation not evidence. It also fails to account for the fact that~~ While some of these barriers are speculative, we are concerned enough to require that, in addition to the fact that Ameritech will continue to be subject to our jurisdiction and to all the dictates of the Act and our rules, conditions designed to promote competition and listed below in this Order apply.

***

Overall, it is important to note that the relevant inquiry is whether SBC "would likely" compete with Ameritech Illinois in the near future. See, e.g., FCC BA/NYNEX Order at para. 138 n. 260. Some federal courts require "clear proof" of entry, while others only require a "reasonable probability", see e.g. FTC v. Atlantic Richfield Co., 549 F.2d 289, 294-295(4th Cir 1977); BOC International Ltd. v. FTC, 557 F.2d 24, 28 (2nd Cir. 1977); Mercantile Tx. Corp. v. Board of Governors, 638 F.2d 1255, 1268-1269 (5th Cir. 1981). We view factors such as SBC's geographic proximity, physical assets, and cellular experience in Illinois as relevant to its "likely" entry. Those factors support Staff's and GCI's position that SBC would act to increase profits in the absence of acquisition, and that such a desire to increase profits would likely bring SBC to Illinois in perhaps 3-5 years.

As to the doctrine's fourth element, we find that the impact from SBC's likely independent entry into Illinois' local exchange market would ~~not~~ be significant. When we examine the ~~various parties~~ Joint Applicants' assertions,

they invariably suggest that SBC's entry would be limited in scope and geared to capture large business customers. We do not believe that SBC's ambitions would be so limited without this merger. ~~While even such entry may benefit competitors, it does not benefit, and may even harm small business and residential customers. At the very least, Staff argues, SBC's entry would shake up the market and engender competitive motion which would be a significant impact, in light of the fact that the market has seen little competitive movement since deregulatory efforts began. We note, however, that Staff does not apply the same reasoning with respect to AT&Ts recent local competitive strategy.~~

There is ~~no~~ significant evidence that SBC would have more of an impact on the Illinois local exchange market than potential entrants like AT&T, MCIW, and Sprint, ~~all of~~ which, while haveing significant technical and capital resources, ILEC experience, and national brand names, cannot match SBC in marketing and technical expertise in building facilities-based local service. SBC already offers vertical services such as Caller I.D. and Call Waiting in other markets and would have an advantage in offering the one-stop shopping for telecommunications services that business and residential customers desire. ~~In other words, the same factors which are ascribed to SBC apply to these entities as well. Even if SBC were to enter the Illinois local exchange market, there is no evidence that it would not do what some other carriers are doing, which is to pursue large business customers only, with no impact on the provision of local exchange services to residential and small business customers. This would not amount to significant entry in our view.~~

4. The HEPOR overestimates the impact that other potential competitors would have on the local residential market by focusing on the financial resources and brand names of AT&T, MCIW and Sprint without considering when that competition is likely to occur.

The HEPOR states that "it is improbable that SBC will be able to single-handedly deconcentrate the market or obtain a significant share of the market anymore than other competitors combination with other entrants", HEPOR at 31. The HEPOR considers merely the potential and not the timeliness for entry of other competitors. As explained above, SBC would have a head start over other non-RBOCs in providing facilities-based local service within 3-5 years. AT&T, MCIW, and Sprint, companies which traditionally are not associated with the provision of local exchange service, have not succeeded in deconcentrating the local

exchange market in the three years since TA96 was passed. Given the continuation of existing barriers to entry, it is unlikely that AT&T, MCIW and Sprint will be more successful at providing local exchange service (especially for residential customers) in the next three to five years. The elimination of SBC, an RBOC with significant local exchange experience, makes it that much less likely that the local exchange market will become deconcentrated in the near future.

With regard to other RBOCs, SBC has a marketing advantage over Bell Atlantic, BellSouth and US West because SBC provides cellular service in the Chicago MSA and local service in southwest Illinois, GCI Brief on Re-Opening at 12-13. The HEPOR revisions recommended by GCI below reflect the diminished impact and delay in entering the market by other potential competitors.

> As mentioned earlier, SBC is ~~not~~ one of only a few potential competitors of Ameritech Illinois. ~~To the contrary,~~ Ameritech Illinois would have at least six major competitors (AT&T, MCIW, Sprint, Bell Atlantic, BellSouth, and US West) after the merger. This number is sufficient and undisputed. (1984 DOJ Merger Guidelines, § 4.133, SBC/Am. Ex. 35.) However, only the three RBOCs would be significant competitors in the local market. ~~The argument that certain firms cannot be considered potential entrants because of some current market presence, however small, is not persuasive.~~ The key inquiry is not only future competitive significance but also timeliness; if AT&T or MCIW have the "potential" to expand their respective market shares in the Illinois local exchange market they must do so within the 3-5 year period that SBC would enter into the market. If they can't, then for purposes of this analysis the~~y~~ir entry is not "timely" and they are ~~both~~ neither actual competitors ~~and~~ nor actual potential competitors. *See, e.g., 1991 Cal. PUC Lexis 629, 177 PUB 462*. The record does not support a finding that given current barriers to entry, AT&T, MCIW or Sprint are likely to have as significant a deconcentrating effect on the local exchange market as would SBC. ~~Indeed, the fact that they already have a toe hold in the market makes them, if anything, even more significant then other potential competitors, that are not currently in the market such as SBC. The presence and visibility of AT&T and MCIW make them the most likely to rapidly capture market share from Ameritech Illinois in the near future.~~

5. The HEPOR **places too much emphasis on AT&T's cable ambitions as a potential competitor in the local exchange market.**

The HEPOR's optimism in suggesting that "AT&T's cable service could be developed to provide local exhange service on a large scale" within 3-5 years, HEPOR at 30, is misplaced. The proposed revisions by GCI in the HEPOR below reflect the fact that AT&T's efforts to enter the local residential market through cable lines are unproven technically and unlikely to meet the timeliness standards set forth in the DOJ guidelines.

The following language should be eliminated on page 31:

> ~~**Nor can we dismiss AT&T's recent mergers and its stated desire to develop a cable alternative to telephone service. This is evidence of the creative and expansive ways that telecommunications providers are changing the markets. AT&T's cable service, in the next three to five years, could be developed to provide local exchange service on a large scale. We are not persuaded by Staff's attempts to minimize the significance of this venture.**~~

The following changes should be made to page 31:

> **In the final analysis, ~~while~~ <u>only</u> SBC could likely enter the local market in the next three to five years~~, it is improbable that SBC will be able to single-handedly deconcentrate the market or obtain a significant share of the market anymore than other competitors combination with other entrants.~~ <u>SBC would have a head start over other non-RBOCs in providing facilities-based local service within 3-5 years. SBC has a marketing advantage over Bell Atlantic, BellSouth and US West because SBC provides cellular service in the Chicago MSA and local service in southwest Illinois,</u>**

3. ENFORCEMENT

QUESTION 12: Reasonable and effective enforcement mechanisms for any condition imposed, including appropriate penalties, economic or otherwise.

We take exception to the HEPOR's conclusion that the Joint Applicants have provided enforcement mechanisms "for any condition imposed" that are "reasonable and effective." The "enforcement mechanisms" described by the HEPOR do not, in fact, amount to any enforcement mechanism at all but simply an agreement to litigate the specific provisions of interconnection agreements when disputes concerning their implementation arise. Such an analysis does not address the Commission's question set forth in the Commission's June 4th letter, which the HEPOR acknowledges defines the scope of this Reopening. HEPOR at 6.

The Commission's conclusion with respect to Question 12 flows from its conclusion with respect to Question eleven. HEPOR at p.117 The Commission's conclusion with respect to Question 11 is limited to an endorsement of the Joint Applicants' commitment to import the "Texas Plan" of interconnection performance measurements/benchmarks, along with associated liquidated damages, to Illinois interconnection agreements. However, as Staff correctly notes, the Joint Applicants' commitment to the "Texas Plan" does not guarantee any particular level of parity with service provided to Ameritech's ILEC's. As both AT&T and Sprint correctly point out, without knowing which specific performance measures will be implemented in Illinois, the Joint Applicants' commitment is too undefined to be meaningful. Therefore, the Commission cannot reasonably rely upon the Joint Applicants' answer to Question 11 in reaching a conclusion to Question 12. Vague commitments to adhere to unidentified performance measures/benchmarks are meaningless and only ensure perpetual litigation in the future.

Consequently, the Joint Applicants' answer to Question 11 does not provide the analytical basis necessary to reach a logical conclusion to Question 12. In particular the HEPOR's reliance upon "various collaborative processes" to resolve disputes before formal litigation does not qualify as an “enforcement mechanism.” As aptly described in AT&T witness Gillan's testimony a "commitment " to "talk about a commitment" is, in fact, no enforcement mechanism at all.

Furthermore, the HEPOR fails to mention any account of GCI's arguments as set forth in their Initial Brief with respect to Commission Question #12. In GCI's Draft Proposed Order, GCI explained that the Joint Applicants' response to Question 12 referred only to enforcement of the Joint Applicants' voluntary commitments, rather than to enforcement mechanisms with respect to “any conditions.” Given GCI witness Selwyn’s testimony on the Joint Applicants' poor track record in meeting their regulatory commitments in Connecticut (SBC) and Indiana (Ameritech), the Commission should take special precautions that any enforcement mechanisms taken forth in this proceeding are sufficiently comprehensive to address all merger conditions

Proposed Language:

> The Commission has reviewed the responses filed by Joint Applicants with respect to the enforcement of the Joint Applicants’ voluntary commitments, as well as the testimony filed in support of those answers. It first must be noted that the Commission’s question addressed enforcement mechanisms “for any condition imposed.” The Joint Applicants’ response, however, refers to “these commitments,” not to “any conditions.” The Commission requires the Applicants to adhere to all conditions, either voluntary or imposed by the Commission.
>
> In an effort to eliminate any ambiguity in this regard, we conclude that Joint Applicants shall file compliance reports with respect to all conditions

imposed by the Commission. The independent auditors, likewise shall address all conditions that are part of the Commission's approval of this merger. The filing of these report with the Commission shall be public filings, with both made available on the Joint Applicants' Internet site. The material contained within these reports shall not be presumed proprietary or confidential. Proprietary and/or confidential treatment may be sought only through a formal request to the commission to be filed 30 days prior to the filing of either report. Commission Staff and interested parties shall then be provided with an opportunity to respond to the request for proprietary treatment. In any request for proprietary/confidential treatment of any such material, the burden shall be on the party proposing proprietary and/or confidential treatment. Opportunity to comment on each report, including the opportunity to present evidence, will be afforded to ICC Staff and interested parties. The Commission will initiate official proceedings to formalize the results of the independent audit, issue findings on the audit results, and assign any penalties due to non-compliance.

III. CONCLUSION

WHEREFORE, the People of State of Illinois, the Cook County State's Attorney's Office and the Citizens Utility Board urge this Commission to conclude that given the additional evidence presented during this reopened proceeding, the Joint Applicants have once again failed to meet their statutory burden under Section 7-204 of the Illinois Public Utilities Act.

If the Commission decides the evidence presented on reopening legally justifies approval of the merger, the above-named parties respectfully request this Commission to impose conditions specifically designed to eliminate or mitigate the risks and adverse competitive and consumer impacts of this reorganization in order to protect the public interest, as described herein above and in the parties respective briefs.

Respectfully submitted,

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